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116998—35

In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 663

JOHN A. SNYDER, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The findings of fact and opinion of the Board of Tax Appeals (R. 23–26) are reported in 29 B. T. A. 39. The opinion of the Circuit Court of Appeals (R. 34–41) is reported in 73 F. (2d) 5.

JURISDICTION

The judgment of the Circuit Court of Appeals, affirming the Board of Tax Appeals, was entered September 18, 1934. (R. 41–42.) A petition for rehearing was denied on October 24, 1934. (R. 42.) The petition for a writ of certiorari was filed Jan-

uary 23, 1935, and granted on February 4, 1935. The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether shares of stock held on margin are capable of identification so that a taxpayer selling part of his holdings may select, as his basis for determining gain or loss, the cost of any particular lot.

2. Whether Article 58, Regulations 74, is valid.

3. Whether, when stock is sold during the taxable year, the taxpayer may have his gain or loss computed without regard to the cost of such stock, the stock having been acquired in an earlier year.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1928, c. 852, 45 Stat. 791, 797, 815, 816, 818:

SEC. 22. GROSS INCOME.

* * * * *

(e) *Determination of gain or loss.*—In the case of a sale or other disposition of property, the gain or loss shall be computed as provided in sections 111, 112, and 113.

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided

in section 113, and the loss shall be the excess of such basis over the amount realized.

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Property acquired after February 28, 1913.*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; * * *.

Treasury Regulations 74:

ART. 58. *Sale of stock and rights.*—When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots cannot be determined, the stock sold shall be charged against the earliest purchases of such stock. The excess of the amount realized on the sale over the cost or other basis of the stock will constitute gain. * * *

STATEMENT

The facts as found by the Board of Tax Appeals (R. 24) may be summarized as follows:

In 1928 and several prior years the taxpayer dealt in stock of the United Gas Improvement Company. He traded through two brokerage houses on margin and pyramided his purchases. Upon a

decline in the market so that his margin fell below the required percentage the brokers reduced his debit balance by sufficient sales to make up the deficiency in the margin. Upon a rise in the market the paper profits were used to increase taxpayer's holdings of the stock. By this method of operation the stock standing to the taxpayer's credit on the broker's books increased during the year from 5,300 shares to 8,000 shares, an increase of 2,700 shares. At the same time his debit cash balance on the broker's books increased from $501,865.59 to $932,822.67, an increase of $430,957.08. These changes were the results of sales by the brokers at various dates throughout the year of a total of 7,900 shares and the purchase of 10,600 shares for the taxpayer's account. Purchases and sales affecting the taxpayer's accounts were entirely through the medium of street certificates handled by the brokers, who debited and credited the taxpayer's account to reflect the transactions. At no time during the year did the brokers, on the one hand, or the taxpayer, on the other, deliver to each other actual stock certificates. The substance of the taxpayer's testimony was that each sale was made in order to increase his margin and in each case where a sale was made it was his intention to sell the last acquired stock first and shortly thereafter to buy back an equivalent amount.

In determining the deficiency in question the Commissioner applied to the taxpayer's stock

transactions the provisions of Article 58, Regulations 74; that is, he applied the various sales of stock during the year against the earliest purchases of stock. (R. 17.) The Board of Tax Appeals approved of this (R. 24–26) and the Circuit Court of Appeals affirmed (R. 34–41).

ARGUMENT

In 1928 the taxpayer traded in United Gas Improvement Company stock through two brokerage houses on margin and pyramided his purchases. At the beginning of the year he had 5,300 shares and during the year he purchased altogether 10,600 additional shares and sold 7,900 shares. In computing his gain the Commissioner held that the marginal sales were not identifiable. He accordingly applied Article 58, Regulations 74, *supra,* and matched the sales against the earlier purchases.

1. The taxpayer intended to sell the last shares acquired by him and contends that this intention was identification of the stock sold sufficient to take the case out of the rule prescribed by the regulation. The case in this respect is practically identical with the case of *Helvering* v. *James L. Rankin, Executor of the Estate of Richard B. Turner, deceased,* now pending before this Court, No. 582, present term. For the reasons set forth in the Government's brief in that case, a copy of which has been served on counsel for the taxpayer in this case, we submit that a mere intent to sell the last stock acquired was not an identification of the stock sold.

In fact, there is less evidence respecting identification in this case than there was in the *Rankin* case. In both cases the taxpayer traded on margin, making identification impossible, and in both cases the taxpayer intended to sell his last acquired stock, but in the *Rankin* case the taxpayer communicated his intention to his broker, whereas in this case no such communication was made. The court below gave effect to this difference, holding in the *Rankin* case that such communication amounted to identification, but holding in this case that the uncommunicated intention did not constitute identification. As pointed out in our brief in the *Rankin* case, since the broker cannot identify the stock sold, it is not apparent how the communication of the taxpayer's intention to the broker can add anything to the intention itself. But should this Court hold in the *Rankin* case that the communicated intention was sufficient identification, we respectfully submit that the mere subjective intent in this case, not communicated to anyone at the time, and not evidenced by any memoranda or book entries of any kind, is not sufficient. To permit the bare intent of the taxpayer to control would make every case of this kind depend entirely upon the undisclosed mental attitude of the taxpayer whether formed at the time of the sale or later, and on whether the taxpayer could convince the court that he had such intent. This would encourage litigation in which the taxpayer would always have the advantage. As pointed out by the court below, the distinction be-

tween the *Rankin* case and this is that in the *Rankin* case the taxpayer tried to give effect to his intent, though, as we view it, the attempt was futile, whereas in this case, the taxpayer did nothing whatever to give life to his intent. For the reasons given by the court below, we submit there was no identification in this case, even though it should be held that there was identification in the *Rankin* case.

2. The taxpayer in this case makes the same argument as does the taxpayer in the *Rankin* case, that if the regulation is held applicable it deprives him of due process of law in that it establishes an irrebuttable presumption and is therefore void under the rule in *Heiner* v. *Donnan*, 285 U. S. 312. (Pet. 21.) As pointed out in our brief in the *Rankin* case, we think the regulation entirely reasonable as applied to marginal transactions where identification is impossible. For the reasons stated in the *Rankin* brief we submit the rule is valid.

Should this Court follow the distinction made by the court below and hold that a communicated intention, as in the *Rankin* case, amounts to identification, but that an uncommunicated intent, as here, does not, then all questions raised by the taxpayer with respect to the validity of the regulation are removed. If such should be the holding, taxpayers in every case could rebut the presumption set up by the regulation by merely following the procedure adopted by the taxpayer in the *Rankin* case. Considered in this aspect the regulation is clearly re-

buttable and *Heiner* v. *Donnan, supra,* can not possibly apply.

3. The taxpayer in this case contends that his stock market operations constituted a trade or business, and that in determining his gain or loss only the "transactions" of the current year are to be considered, without regard to "transactions" of prior years. (Pet. 2, 16–19.) As we understand his argument, it is that sales made during the tax year are to be charged only against purchases of that year. At the beginning of the tax year the taxpayer's account was long 5,300 shares. During the year he bought 10,600 shares and sold 7,900 shares and his position appears to be that the 7,900 shares sold are to be charged against the 10,600 shares purchased during the year, since only "transactions" of the current year are to be considered. As stated by the court below, there is nothing substantial in this defense. (R. 37.)

Sections 111 (a), 112 (a) and 113 (a) of the Revenue Act of 1928, *supra,* prescribe how gain or loss from the sale of property is to be computed, namely, by comparing the selling price of the property with its cost, no matter whether the property was acquired in the year of sale or in an earlier year. Until the shares, whenever purchased, are sold there is neither gain nor loss. A gain springs from the sale and the tax is imposed on the gain in the year of sale to the full extent of the gain, even though the gain is attributable to appreciation in value of the property since its acquisition in an

earlier year. Cf. *MacLaughlin* v. *Alliance Ins. Co.*, 286 U. S. 244. The extent of the gain in this case depends on the cost of what was sold, which in turn depends upon what shares were sold, the last purchased, or the first purchased, or shares intermediate the two. The burden is on the taxpayer to show the cost of what was sold. Identification being impossible, the regulation is applicable.

The taxpayer's position ignores the question of how the subsequent gain or loss from the sale of the 8,000 shares held at the end of the taxable year is to be treated, nor does he suggest how the gain in 1928 would be treated in the event he had sold more shares during the year than he purchased, i. e., in the event he had sold part of the 5,300 shares held at the beginning of the year. This serves to demonstrate the unsoundness of his position.

CONCLUSION

The decision of the Circuit Court of Appeals should be affirmed.

Respectfully submitted.

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